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UNCLAS SECTION 01 OF 02 GUANGZHOU 000475

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SUBJECT: Draft Labor Contract Law: Companies are Concerned but Cautious

**¶1.** (U) SUMMARY: Most foreign companies with offices in South China have negative impressions of China's draft labor contract law, but few companies believe the law will significantly impact their growth plans in China, according to a survey jointly released on April 11 by Hewitt and Baker & McKenzie. Most companies are uncertain of the implications of the law, with one quarter having done nothing at all to prepare. Companies that lack employee representation plan to establish either formal or informal representative bodies. European companies are less concerned with the law than U.S. companies because of similarities with European labor laws. END SUMMARY

Background of the Survey

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**¶2.** (U) A total of 436 companies with offices in South China participated in the survey on February 7-14, 2007. Three-quarters of respondents were wholly foreign-owned companies and half were in manufacturing, with a wide range in terms of company size. Hewitt and Baker & McKenzie conducted the survey and discussed the results at an April 11 conference in Guangzhou. Hewitt's Christian Doeringer said company response to the survey was unprecedented, with 250 companies completing the survey within the first day. The National People's Congress will reportedly finalize the draft labor contract law in summer 2007, with implementation in late 2007.

Impact of the Law, Actions Taken

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**¶3.** (U) Slightly over one-half of companies said the new law will have a negative impact on their business, with the rest neutral. Almost no companies believe the law will positively affect their business. Nevertheless, very few companies have revised their growth plans in China - suggesting that they expect growth to continue despite the new law. European companies are generally less concerned than U.S. companies with the new law, according to Hewitt's Doeringer, because of provisions on layoffs, duration of contracts, and unions that reflect European labor law.

**¶4.** (U) Companies are highly uncertain of the implications of the new law, according to the survey. Most companies have not yet decided how to adapt company operations to comply with the law, which contains no grandfathering provisions. Most HR sections have briefed senior management about the law and one-third have sought the help of outside consultants. However, more than a quarter of companies have done nothing at all. This is particularly true for smaller companies.

Employee Representation and Unions

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**¶5.** (U) Approximately half of the respondents currently have no employee representation in their companies. Manufacturing companies

are more likely than service providers and small companies to have either formal or informal employee organizations. Those companies that lack employee representation are split 50-50 on whether to establish formal unions or informal representative bodies to comply with the draft law. Only a small number of companies have plans in place to address the potential new requirement to negotiate a collective agreement with their workforce - and most do not understand the implications of this provision.

**16. (U)** Under the new law, employers must consult with employee representatives before making changes to employment policies. Doeringer said this will give employee organizations, many of which are currently little more than social groups, more input on compensation issues. How much input is unclear, as the draft law uses the term "consultation" (the first draft used the term "approval"). Baker & McKenzie's Jonathan Isaacs said the drafters left this provision vague in order to reduce criticism from business. On a separate but relevant issue, several companies noted at the conference that they have recently been pressured to set up unions by the All-China Federation of Trade Unions, which is in the middle of a campaign to organize more unions in foreign-invested enterprises.

#### Employment Contracts and Temporary Workers

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**17. (U)** The draft law will encourage the use of open-term contracts or longer fixed-term contracts by limiting the number of fixed-term contracts per employee to two. Most companies surveyed use fixed-term contracts that range from one to three years. Service companies and small companies are more likely than manufacturing companies to use open-term contracts. U.S. companies are more likely than European companies to use open-term (permanent)

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contracts. To comply with the new law, almost half of companies plan to adjust their mix of fixed-term, open-term, and temporary employees. One-third of companies have no plans to make changes.

**18. (U)** Three-quarters of respondents use temporary (seconded) employees. Despite provisions in the draft law that require more expenditures on training and benefits to temporary employees, few companies plan to reduce the number of temporary workers or stop using them altogether. However, a majority of companies plan to negotiate new agreements with labor agencies to comply with the law. The draft law also reduces the maximum hours of part-time employees from 30 to 24. Only one-third of companies plan to hire part-time workers in the future (the survey did not say how many companies currently hire part-time workers).

#### Firing Workers

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**19. (U)** Two-thirds of companies said the law's provisions on mass layoffs will not affect their operations in the foreseeable future. The new law requires that, in cases of mass layoffs, companies must first fire employees whose social circumstances are least affected by the job loss (people without dependents). Doeringer said similar provisions exist in Germany - thus European companies are less concerned about this provision than U.S. companies. In addition, because more open-ended contracts will be used under the law, companies will need to provide stronger evidence of unsatisfactory performance before firing workers. Though the draft law requires more extensive record-keeping in general, Doeringer said documentation related to job performance will be particularly burdensome.

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